BEFORE THE

Federal Communications Commission

WASHINGTON, D.C. 20554

In the Matter of	)	
	)	
Access Charge Reform	)	**CC Docket No. 96-262**
	)	
Price Cap Performance Review for Local Exchange Carriers	)	**CC Docket No. 94-1**
	)	
Transport Rate Structure and Pricing	)	**CC Docket No. 91-213**
	)	
End User Common Line Charges	)	**CC Docket No. 95-72**
	)	

REPLY OF THE AMERICAN PETROLEUM INSTITUTE TO PETITIONS FOR RECONSIDERATION

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EXECUTIVE SUMMARY

The Telecommunications Act of 1996 rejects the long-standing practice of obligating one end-user class to subsidize another for the ultimate benefit of the ILEC. Nonetheless, under the *Access Charge Reform Order,* multiline business line customers will be obligated to pay non-cost-based SLCs and PICCs which have been inflated and/or set solely to subsidize lower assessments on residential and single-line business line customers. These and other aspects of the *Order* appear designed to ensure ILEC revenue recovery - as opposed to cost recovery - even though competitive markets do not guarantee revenue recovery for any player. As numerous petitioners demonstrate, these revenue-recovery policies impede competition and result in excessive rates.

Allowing ILECs an exogenous adjustment for USF contributions is one such policy that leads to competitive inequities, as AT&T demonstrates. AT&T's proposed fix, a mandatory end user surcharge on all interstate retail revenues, is impermissible under Section 254. A more appropriate fix in light of the Commission's reliance on "marketplace forces" is to eliminate the ILECs' ability to recover their USF contributions as exogenous adjustments. In no case should the Commission extend the ILECs' competitive advantage by granting USTA's Petition to exempt application of the X-Factor to the exogenous adjustment.

The Commission should grant the numerous Petitions seeking the elimination or a reduction in the level of the multiline business line PICC. This PICC, which guarantees ILEC common line revenue recovery by requiring multiline business line customers to subsidize residential and single line business line users, represents a return to discredited residual rate-making principles. As many petitioners observe, the multiline business line PICC is discriminatory, at odds with the principles of cost-causation, and constitutes the very type of subsidy that the Commission has been charged with eliminating. Similarly, AT&T's proposal to increase the multiline business line SLC to recover items such as corporate operations expenses and telecommunications uncollectibles is an attempt to impose residual ratemaking principles and should be rejected.

Even if the multiline business line PICC is reduced, the Commission should take action to avoid unintended rate shock for Centrex users by adopting a trunk-equivalency approach to PICC assessments for these customers, as many petitioners urge. The Commission should also extend the transition period applicable to call set-up charges for an additional two years, until July 1, 2000. Given that the record contains widely varying estimates of the costs of call set-up, this extension helps ensure that rates ultimately borne by end users will reflect those ILEC costs actually incurred.

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To: The Commission

REPLY OF THE AMERICAN PETROLEUM INSTITUTE TO PETITIONS FOR RECONSIDERATION

The American Petroleum Institute (API), by its undersigned attorneys, hereby respectfully submits this Reply to Petitions for Reconsideration filed in response to the *First Report and Order* adopted by the Federal Communications Commission (the Commission) in the above-captioned proceeding, released May 16, 1997.[1]

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1 *Access Charge Reform,* CC Docket No. 96-262, First Report and Order, FCC 97-158 (rel. May 16, 1997) (*Order or Access Charge Reform Order).* Notice of the filing of Petitions for Reconsideration was published in the Federal Register on August 1, 1997 (62 Fed.Reg.41386-87).

I. REGULATORY EFFORTS TO ENSURE ILEC REVENUE RECOVERY PENALIZE CONSUMERS AND COMPETITORS

The Commission has described its *Order* as implementing a market-based approach with a prescriptive backdrop. This reliance on marketplace forces, however, is difficult to reconcile with regulatory "reforms," such as increasing caps on subscriber line charges (SLCs) or establishing presubscribed interexchange carrier charges (PICCs), that work only if the overwhelming majority of consumers has no viable choice of local service provider.

In many respects, the "reforms" adopted by the Commission appear to reflect the principles of monopoly pricing. Under the *Order,* multiline business line customers will be obligated to pay non-cost-based SLCs and PICCs inflated and/or set solely to subsidize lower assessments on residential and single-line business line customers, thereby ensuring that the ILEC recovers its common line revenue requirement. Such charges, of course, would be unsustainable in a competitive environment.[2]

Similarly, although competitive markets do not guarantee revenue recovery for any player, the *Order* appears designed to ensure revenue recovery - as opposed to cost recovery - for incumbent local exchange carriers. Given that the incumbent carriers have long enjoyed virtually 100 percent market share, regulatory decisions that reflect a policy

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[2] The Competitive Telecommunications Association makes a similar argument with respect to tandem switching: "It is clear that the current interstate tandem switching rates are reasonably close to market-driven, cost-based levels, while the rates that the FCC has directed the ILECs to implement as of January 1, 1998 are grossly excessive." Expedited Petition for Reconsideration of Competitive Telecommunications Association at 8.

of ensuring *revenue* recovery for these dominant players thwart the development of competition and ensure inflated rates.

The Telecommunications Act of 1996 (1996 Act) mandates that, in the pro-competitive, de-regulatory environment, ILEC revenue recovery no longer will be guaranteed. In a resounding rejection of traditional rate design notions, the 1996 Act envisions cost-based rates for competitors, universal service support for *any* eligible telecommunications provider, and the use of that support "only for the provision, maintenance, and upgrading of facilities and services for which support is intended." With the statutory directive that telecommunications *carriers* and *providers* contribute to "specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service," the Act rejects the long-standing practice of obligating one end-user class to subsidize another for the ultimate benefit of the ILEC.

As the judicial battles spawned by implementation of the 1996 Act continue and escalate, it should be clear that the ILECs generally espouse a belief in their entitlement to revenue levels at least comparable to those earned under rate-of-return regulation. The apparent effect of the *Order* is to appease these ILEC interests, at the expense of end-users and competitors, by loading upon core ILEC monopoly services rates and charges that bear no relation to cost. Given the directives of the 1996 Act, the Commission should reconsider those aspects of its *Order* that require ILEC customers and competitors to shoulder rates and charges designed to ensure the ILEC's revenue recovery, rather than its cost recovery. The Commission should adopt rates and charges payable by users and competitors that reflect only those costs demonstrably incurred by the ILEC in providing the facilities and services and should eliminate all end-user charges, direct and indirect, that function as subsidy mechanisms.

II. THE COMMISSION SHOULD REJECT THE NOTION OF A MANDATORY END USER SURCHARGE

AT&T's Petition includes a compelling analysis demonstrating that, although the Commission requires that universal service support be assessed in a competitively neutral manner, "the recovery of this assessment is not competitively neutral."[3] A significant contributor to the inequity is the Commission's decision to allow ILECs to assign their USF support obligation as an exogenous cost-causative adjustment to those price cap baskets containing interstate end user telecommunications service revenues: the common line, trunking, and interexchange baskets, based on the relative proportion of end user revenues.[4]

Under the AT&T analysis, of the $4.65 billion in anticipated 1998 USF funding, $1.35 billion will be assessed on ILECs based on their relative end user telecommunications service revenues. Roughly 85 percent, or $1.17 billion of this $1.35 billion, would be allowed to be recovered as an exogenous adjustment to the Common Line basket. Given the controlling formulas and rules,

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[3] The discussion and proposal appear to straddle both the Commission's *Access Reform Order* and its *Universal Service Order (Federal-State Joint Board on Universal Service Reform*, CC Docket No. 96-45, Report and Order, FCC 97-157 (rel. May 8, 1997). AT&T Petition at 2-3.

[4] *Access Charge Reform Order* at ¶ 379.

> of the $1.17 billion of ILEC USF obligations that flow to the Common Line basket, the entire amount will be recovered from access charges paid by IXCs (through the flat-rated presubscribed interexchange carrier charge ('PICC') and the usage-sensitive Carrier Common Line Charge ('CCL')). In essence, this $1.17 billion of assessment on *retail* revenues has been transferred to wholesale services. Thus, the *effective* USF support obligation on the ILECs' retail services is only $.18 billion ($1.35 billion less $1.17 billion), whereas the IXCs' retail services would have to recover $3.72 billion ($2.55 billion of IXC retail revenue assessment plus $1.17 billion of ILEC retail revenue assessment).[5]

AT&T concludes that the appropriate Commission action should be to reconsider the rules that lead to such inequitable results and implement, instead, an explicit, mandatory end user surcharge on all interstate retail revenues.

While AT&T's analysis of the comparative impact on ILECs and IXCs is correct, its proposed fix is not, as a review of Section 254 reveals. Section 254(d) expressly provides that every telecommunications carrier that provides interstate telecommunications *shall* contribute to the universal service mechanisms established by the Commission. The Commission is expressly authorized to exempt those carriers whose contributions would be *de minimis*. It is also expressly authorized to impose the universal service contribution requirement son "[a]ny other *provider* of interstate telecommunications." Nothing in the 1996 Act empowers the Commission to impose universal service contributions on end users. Any attempt to do so - either directly or

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5 AT&T Petition at 3-4; emphasis in original.

indirectly, by implementation of a "mandatory end user surcharge" - would exceed the Commission's authority.

Perhaps the simpler solution to AT&T's concern, and one more appropriate in light of the Commission's reliance on marketplace forces, would be to eliminate the ILECs' ability to recover their USF contributions as exogenous adjustments to the various baskets. Under this approach, all carriers and providers of retail telecommunications services would be treated similarly. Retaining the exogenous adjustment represents yet another instance in which the Commission's rules allow ILECs to recover their revenue requirements at the expense of consumers and competitors. In no case, however, should the Commission grant the reconsideration request of the United States Telecommunications Association (USTA). USTA contends that application of the X-Factor to USF contributions will reduce the exogenous adjustment and result in an insufficient recovery of USF contributions. USTA apparently fails to recognize that the ILECs, alone, enjoy the preferred and enviable position of guaranteed recovery of USF contributions - a position enjoyed by no other class of carrier. The Commission should not enlarge the scope of this preferential treatment.

III. THE MULTILINE BUSINESS LINE PICC SHOULD BE REDUCED OR ELIMINATED

A number of petitioning parties urge the Commission to eliminate multiline business line PICCs or, at the very least, reduce the charge to that assessed against residential and single-line business lines. These parties primarily represent the interests of smaller interexchange carriers, who urge reconsideration of this issue to avert irreparable economic harm to their own businesses and to interexchange competition generally.[6]

These parties correctly identify the failings of the multiline business line PICC. Among other things, this PICC is discriminatory vis-a-vis other classes of customers, squarely at odds with the principles of cost-causation articulated by the Commission, and constitutes the very type of subsidy that Congress directed the Commission to eliminate.

Creation of the multiline business line PICC represents a return to residual rate-making, a regulatory technique that is inconsistent with price cap regulation and discredited by the 1996 Act. According to the Commission, the multiline business line PICC will be assessed to cover a revenue shortfall unrelated to the cost of the service provided to multiline business line users: it will ensure "the recovery of common line costs that incumbent LECs incur to serve single-line customers" and "avoid an adverse impact on residential customers."[7]

Consumers and competitors will be penalized so long as a primary regulatory objective remains guaranteed revenue recovery for incumbent carriers - particularly for those large ILECs subject to the FCC's price cap regime. This objective is incompatible

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6 Among these petitioning parties are trade organizations such as America's Carriers Telecommunications Association (ACTA), the Competitive Telecommunications Association (CompTel), and the Telecommunications Resellers Association (TRA), as well as individual carriers, such as KLP, Inc., d/b/a Call-America andU.S. Long Distance, Inc. Other parties, such as Sprint Corporation, identify unresolved issues associated with PICC implementation.

7 *Order* at ¶ 101.

with both the pro-competitive, de-regulatory mandate of the 1996 Act and the healthy earnings that these carriers typically are enjoying. Such an objective, moreover, impedes the public interest by inflating rates, erecting obstacles to competitive entry, and slowing the development of innovative services that market entrants are likely to offer. The Commission should reconsider its decision and eliminate the PICC for all customers. Alternatively, to remove the discriminatory taint, it should establish a single PICC rate applicable to all ILEC common line customers.

IV. MULTILINE BUSINESS LINE SLCS SHOULD NOT BE INCREASED

Jumping on the residual rate-making bandwagon, AT&T urges the Commission to increase the SLC caps applicable to multiline business lines, so that these end user charges may also recover LEC retail marketing expenses and "direct retail customer service expense, indirect retail expense, corporate operations expense, and telecommunications uncollectibles." AT&T reasons that "*all* of these expenses are avoidable retail costs that should not be recovered from wholesale services, such as access."[8]

AT&T's unsubstantiated assertion offers no basis upon which to increase multiline business line SLCs. Indeed, corporate operations expense and uncollectibles may be as readily allocated to wholesale services as retail. Moreover, while Section 252 mandates wholesale rates that exclude "avoided" costs, the Commission's orders do not extend that standard to access services purchased by interexchange carriers.

8 AT&T Petition at ¶ 9 (emphasis in original).

The Commission's *Order* subjects multiline business line customers to significant and continuing rate increases. These rate increases were adopted despite Congressional and consumer expectations that the 1996 Act would lead to rate *decreases.* No basis exists for the additional rate increases contemplated under the AT&T proposal.

V. PICC ASSESSMENTS FOR CENTREX CUSTOMERS SHOULD BE BASED ON A TRUNK-EQUIVALENCY BASIS

A number of Petitioners, recognizing the unique circumstances of Centrex users, urge the Commission to modify its rules. The International Communications Association (ICA) recommends that PICCs be applied on the same per-line basis as the end user common line charge (EUCL). The County of Los Angeles recommends applying PICCs to Centrex lines on a PBX-trunk equivalency basis, although it also supports reducing the multiline business line PICC to the level of residential and single line business line PICC. Similarly, USTA recommends the use of a line-to-trunk equivalency relationship.

For the reasons explained in these petitioners' filings, Centrex arrangements - which typically substitute for PBX arrangements - will be subjected to disproportionately higher PICC costs than customers of PBX systems. As the County of Los Angeles details, PICC implementation on a per-line basis will engender tremendous rate shock. The prevalence of long-term contracts and the difficulties associated with shifting to PBX arrangements further complicate the picture.[9]

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[9] Many Centrex customers are governmental subdivisions that rely on Centrex to avoid the capital expenditures associated with PBX installations. PBX arrangements may not represent a realistic alternative to Centrex for these customers.

In response to these concerns, in the event the Commission retains the PICC, it should remedy the inequity between Centrex and PBX customers and apply Centrex PICCs on a trunk-equivalency, rather than station-line, basis.

VI. THE COMMISSION SHOULD EXTEND THE TRANSITION PERIOD ESTABLISHED FOR IMPLEMENTING CALL SET-UP CHARGES

The Ad Hoc Telecommunications Committee and various financial service providers, collectively referred to as "User Parties," and CompuServe Incorporated urge the Commission to extend until July 1, 2000 the transition period before implementation of call set-up charges.

Record evidence supports a three-year moratorium on call set-up charges. Comments filed by the financial service providers proposed a transition period of 36 months. According to the User Parties, commenting parties neither objected to a transition period nor suggested that a three-year period was unreasonable.[10] Given the parties' valid considerations and the absence of record opposition, the Commission should grant these limited petitions.

Further support for granting the requested reconsiderations can be found in the Petitions of the Competitive Telecommunications Association (CompTel) and WorldCom, Inc. These parties urge reconsideration of aspects of the *Order* pertaining to

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10 Petition for Partial Reconsideration on Behalf of Ad Hoc Telecommunications User Committee, First Data Corporation, Bankers Clearing House, The New York Clearing House Association, MasterCard International Incorporated, and VISA, U.S.A., Inc. at 4.

rate structure changes applicable to common channel Signaling System 7 (SS7).[11] Their concerns are relevant, for as the Commission recognizes, "[a]mong price cap carriers today, most call setup is performed with out-of-band signalling, generally using the SS7 signalling network."[12] Given that the record contains "widely varying estimates of the costs of call setup," an extension helps ensure that the rates ultimately borne by end users will reflect the costs actually incurred in call set-ups.[13]

WHEREFORE, THE PREMISES CONSIDERED, the American Petroleum Institute respectfully urges the Federal Communications Commission to maintain and further the pro-competitive, de-regulatory policies of the Telecommunications Act of 1996 by taking action consistent with the views expressed herein.

Respectfully submitted,

AMERICAN PETROLEUM INSTITUTE

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Dated: August 18, 1997

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11 Expedited Petition for Reconsideration of Competitive Telecommunications Association at 24-25; Petition for Reconsideration of WorldCom, Inc. at 21-22.

12 *Order* at ¶ 137.

13 *Id.*

CERTIFICATE OF SERVICE

I, Cassandra Hall, do hereby certify that on this 18th day of August, 1997, copies of the foregoing Reply of the American Petroleum Institute to Petitions for Reconsideration were mailed by U.S. First Class Mail, postage prepaid, to the following persons:

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